

SOUTH DURANGO SANITATION DISTRICT
FINANCIAL STATEMENTS AND REPORT OF
INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

December 31, 2018 and 2017

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

February 13, 2019

To the Board of Directors
South Durango Sanitation District

Report on the Financial Statements

We have audited the accompanying statements of net position of South Durango Sanitation District as of December 31, 2018 and 2017, and the related statements of revenues, expenses, and changes in net position, the statement of cash flows, and the notes to the financial statements for the years then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of South Durango Sanitation District as of December 31, 2018 and 2017, and the changes in financial position, and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise South Durango Sanitation District's basic financial statements. The supplemental information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The supplemental schedules are the responsibility of management and were derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplemental schedules are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

 **et Co., LLC**

SOUTH DURANGO SANITATION DISTRICT
Management's Discussion and Analysis
December 31, 2018

The management of the South Durango Sanitation District (the "District"), has provided this narrative overview and analysis of the financial affairs of the District for the fiscal year ended December 31, 2018 as part of the District's audited Financial Statements.

OVERVIEW OF THE FINANCIAL STATEMENTS

This report consists of three parts: management's discussion and analysis, basic financial statements, and notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements.

BASIC FINANCIAL STATEMENTS

Statement of Net Position. The statement of net position includes all the District's assets and liabilities, with the difference between the two reported as *net position*. It provides information pertaining to the nature of the District's current assets and utility plant in service (assets) and its current and non-current obligations (liabilities). The statement also provides the basis for determining the overall financial health of the District including liquidity and financial flexibility.

Statement of Revenues, Expenses and Changes in Net Position. The statement of revenues, expenses and changes in net position includes all the revenues and expenses. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal years. These statements measure the success of the District's overall operation and can be used to determine if the District's user fees, tap fees and other charges are adequate to cover expenses and develop sufficient reserves.

Statement of Cash Flows. The statement of cash flows presents information concerning the District's cash receipts and cash payments during the year. The statement reports the cash receipts, cash payments and net cash from operating, non-capital financing, capital and related financing activities and investing.

FINANCIAL HIGHLIGHTS

1. The District's net position on December 31, 2018 totaled \$6,580,061. Net position was approximately \$950,000 higher than the prior year due primarily to an increase in net investment in capital assets. This increase was primarily the result of increases in cash and investments and the early redemption of long-term debt made possible in part by substantial increases in cash from non-capital financing activities (tap fees).
2. In 2018 Operating Expenses totaling \$851,505 exceeded Operating Revenues of \$619,390 resulting in an operating loss of \$232,115. The 2018 operating loss includes depreciation, amortization and other non-cash adjustments of \$288,249.

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Management's Discussion and Analysis
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After deducting non-cash adjustments, the net cash provided by operating activities was \$56,134.

3. Cash receipts from tap fees were \$1,199,500 in 2018, an increase of more than \$600,000 over 2017 tap fee revenue. The District projects substantial tap fee revenue again in 2019 as growth in the service area continues.

FINANCIAL ANALYSIS OF THE SOUTH DURANGO SANITATION DISTRICT

The true picture of the financial health of the District must be tempered with the operational theory and financial control that is practiced on a daily basis by the District.

FINANCIAL POLICY PRIORITIES

The financial goal of the District is to operate in a cost-efficient manner that is similar to the practices of private enterprise. The Board of Directors of the District annually reviews its financial policies to assess their impact upon financial activities. Policies that affected financial activities are:

1. Growth pays its own way;
2. Cost of administration and operations are funded from user fees;
3. User fees will fund a portion of capital improvement costs when it is determined that the improvement is needed to serve current customers or when tap fees are not sufficient; and,
4. Tap fees are used for capital improvements or debt service for capital improvements that are required to serve new customers.

In order to develop and monitor financial policies that adhere to the financial policy priorities, the District completed a comprehensive master plan in 2003. The primary components of the master plan were a long-range Capital Improvement Plan (CIP) that identified capital improvements that would be needed over the next 20 years in order to meet projected demand for service. The second primary component of the master plan was a financial plan which included a model to project the amount of plant investment fees (tap fees) necessary to generate the funds needed to make the improvements recommended in the CIP. In 2004 the District commenced the first major step in the CIP, the Phase 1 expansion of the wastewater treatment facility. Some continued expansion and upgrades of the collection system were commenced in 2005 and completed in 2007. The collection system now has adequate capacity for all foreseeable growth within the projected service area for at least the next 40 years.

The Phase 1 wastewater treatment plant expansion and Grandview interceptor line upgrade were funded by the District's 2004 Series Sewer Revenue Bonds in the amount of \$4,645,000 and District capital reserves. The bonds were fully paid in 2010.

The District's 2006 Series Revenue Bond in the amount of \$2,000,000 was issued to pay for an upgrade of the District's other main interceptor line which serves the South Durango area. The bond is backed by a pledge of user fees and was restructured in 2009 to reduce debt service

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payments by delaying the repayment of principal. It was restructured again in 2010 with a 15-year repayment schedule. Due to the availability of tap fee revenue the bond was fully repaid in 2018.

The Phase 2 expansion was completed in December 2012. The Phase 2 expansion was paid for with a \$250,000 energy impact grant, an \$800,000 loan from the Colorado Water Resource and Power Development Authority through its Water Pollution Control Revolving Loan program and the balance from District reserves.

As a result of these capital projects the District now has substantial capacity in its collection and treatment system to serve the additional demand which is anticipated in the District's service area in the next several years. The tap fees from new customers will enable the District to repay the bonds and the loan which were used to finance the projects and to accumulate capital reserves for the next expansion.

In 2014 the District completed an analysis of its tap fee structure. That analysis showed that the District standard of wastewater flows of 250 gallons per day (gpd) for each tap was much higher than actual flow records indicated. As a result, the District lowered its standard for each tap to 180 gpd. This is consistent with industry trends due to increased water efficient plumbing fixtures that produce lower flows and general trends toward water conservation by customers. Because of this change the District was able to lower its tap fee by a proportionate amount. The unused capacity in the treatment system based on the new standard will allow for the sale of additional taps. The sale of additional taps at a lower rate will produce the same capital revenue for the District.

The District authorized the development of an updated master plan in 2017 currently scheduled for completion in 2019. The updated master plan will provide an evaluation of the existing wastewater collection and treatment system of the District to evaluate current and projected capacities necessary to meet the projected growth scenarios recently developed and provided by the City of Durango. Once completed the master plan will provide a technical and economic framework for dealing with existing and new service demands.

Day-to-Day Operational Control of the District

For operational control, the District has segmented its budget into two primary categories: (i) operating expenses including include costs for sewage collection, sewage treatment and administration; and (ii) non-operating expenses consisting of capital projects, debt service for bonds and loans used to fund capital projects, and lease purchase obligations for funding equipment used in daily operations. This allows the District to track operating and non-operating revenues and expenditures to determine if the District's financial policy priorities are being achieved. Based on current growth trends and projections the District will be able to pay non-operating expenses from non-operating revenues (tap fees) except where those expenses are properly allocated to capital projects serving existing customers or lease purchase expenditures for equipment and should be paid with user fees.

SOUTH DURANGO SANITATION DISTRICT
Management's Discussion and Analysis
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The District's day-to-day operational control involves many levels of planning, forecasting, and budgeting. Revenues and expenses are allocated to specific functions of the District. The staff presents monthly financial reports to the District Board of Directors. The reports contain revenue and expenditure comparisons to the adopted budget. It is an essential tool for the District's long-range financial planning efforts.

Financial Analysis

Net Position

A summary of the statement of net position is included as Table A which appears below. The District's net position (the difference between assets and liabilities) is one way to measure the financial health of the District. Increases or decreases in the District's net position can be indicators of improving or deteriorating financial health. This, coupled with factors such as population growth and regulatory or policy changes, provide an integrated assessment of the District's health.

TABLE A
Summary Statement of Net Position

	2018	2017
Current assets	\$ 726,114	\$ 462,914
Net utility plant in service	<u>6,786,353</u>	<u>7,054,711</u>
Total assets	\$7,512,467	\$7,517,625
Current liabilities	\$ 167,877	\$ 310,298
Long-term liabilities	<u>764,529</u>	<u>1,577,047</u>
Total liabilities	\$ 932,406	\$1,887,363
Net position:		
Invested in capital assets (net)	\$5,929,289	\$5,252,294
Restricted for debt service	135,731	115,408
Unrestricted	<u>515,041</u>	<u>262,561</u>
Total net position	\$6,580,061	\$5,630,262

From December 31, 2017 to December 31, 2018, total assets were unchanged. Total liabilities decreased by \$954,957 as a result of the reduction in existing long-term debt. The overall effect was an increase in total net position which is likely to continue increasing from tap fee revenue and reductions in long term debt in future years.

Revenues, Expenses and Changes in Net Position

Table B shows the revenues, expenses and changes in net position for 2017-2018 for the District. Table B demonstrates that immediate financial needs are being budgeted and can be reasonably expected to be met. On a year to year basis, the District plans to operate in accordance with its

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financial policies. Tap fee revenue is expected to provide sufficient revenue in future years to pay all debt service except any portion which the Board has determined is properly allocated to existing customers.

Non-cash expenditures such as depreciation are not always covered by operating revenue. When no tap fee revenue was available, user fee revenues were used to pay debt service so the amount available to cover depreciation was reduced. Future tap fee revenue is projected to be substantial and should provide adequate funds for payment of debt service, so operating revenue in excess of operating expenses is now available to fund reserves for depreciation. The District is also increasing budgeted amounts for equipment which is projected for replacement with a useful life of less than 10 years.

The District reviewed its operating budget in 2015 and determined that a decrease in monthly user fees was appropriate since user fee revenue was almost 150% of the total of all operating expenses except depreciation. That has reduced operating revenue coverage to about 125%. It may be necessary to increase user fees to maintain or increase that ratio in future years as operating costs increase.

TABLE B
Condensed Statements of Revenues, Expenses and Changes in Net Position

	2018	2017
Total operating revenues	\$ 619,390	\$ 607,826
Total operating expenses	<u>851,505</u>	<u>768,800</u>
Operating income	(232,115)	(160,974)
 Non-operating revenue	 \$ 1,216,968	 \$ 592,904
Non-operating expense	<u>(35,054)</u>	<u>(72,229)</u>
Total non-operating revenue	1,181,914	520,675
 Net income	 \$ 949,799	 \$ 359,701
 Beginning net position	 \$ 5,630,262	 \$ 5,270,561
Ending net position	\$ 6,580,061	\$ 5,630,262

Table B shows a substantial increase in net position of the District from 2017 to 2018. As noted in the highlights, this increase is primarily the result of strong tap fee revenues. The District anticipates its financial statement will show an increase in net position in future years provided reasonable growth continues.

ECONOMIC FACTORS; NEXT YEAR'S BUDGET AND RATES

The Board of Directors and the management of the South Durango Sanitation District considered many factors when it established the budget for 2019. Projected revenue from user fees and changes in operating costs were evaluated and considered before a final budget was adopted. The 2019 budget projects an increase in use fee revenue due to an increase in the number of

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customers. The budget also projects substantial tap fee revenue based on development projects in the District service area currently planned for 2019 although slightly less than the amount received in 2018.

The Capital Improvements Plan (CIP) of the District is updated based on revised cost estimates, timing of capital improvements and interest costs for capital financing. If necessary, the rate for tap fees is adjusted to ensure that the District's Financial Policy Priorities continue to be achieved. The change in the District standard for gpd/tap as discussed above resulted in an adjustment. No additional adjustments are projected for the next few years. As part of the master plan that will be completed in 2019 the CIP will be updated and fees will be adjusted as necessary to meet the projections of the financial plan.

CONTACTING THE DISTRICT

This financial report is designed to provide our residents, customers, investors, and creditors with the general overview of the District's finances and demonstrates the District's accountability for the money it receives. If you have any questions concerning this report or need additional information please contact the South Durango Sanitation District at PO Box 2024, Durango, Colorado 81302-2024.

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South Durango Sanitation District
STATEMENTS OF NET POSITION

December 31,

	2018	2017
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 260,805	\$ 71,028
Investments	378,502	318,777
Accounts receivable	54,148	50,869
Inventory	615	615
Due from Loma Linda Sanitation District	7,272	7,530
Due from developers	24,772	14,095
Total current assets	726,114	462,914
Utility Plant in Service		
Land and easements	243,120	243,120
Furniture and fixtures	5,035	5,035
Well	15,124	15,124
Plant and improvements	10,663,865	10,637,715
Storage building	20,828	20,828
Equipment	590,384	576,312
	11,538,356	11,498,134
Less accumulated depreciation	(4,752,003)	(4,443,423)
Net utility plant in service	6,786,353	7,054,711
Total assets	<u>\$ 7,512,467</u>	<u>\$ 7,517,625</u>
LIABILITIES AND NET POSITION		
Liabilities		
Current Liabilities		
Accounts payable	\$ 19,222	\$ 30,374
Accrued interest	1,284	4,255
Accrued compensated absences	3,052	-
Revenue received in advance of service	51,784	50,317
Current portion of long-term debt	37,322	171,586
Current portion of capital lease obligation	55,213	53,757
Total current liabilities	167,877	310,289
Non-current liabilities		
Long-term debt, net of current portion	559,259	1,316,582
Capital lease obligation, net of current portion	205,270	260,492
Total non-current liabilities	764,529	1,577,074
Total liabilities	932,406	1,887,363
Net Position		
Net investment in capital assets	5,929,289	5,252,294
Restricted for debt service	135,731	115,408
Unrestricted	515,041	262,560
Total net position	6,580,061	5,630,262
Total liabilities and net position	<u>\$ 7,512,467</u>	<u>\$ 7,517,625</u>

The accompanying notes are an integral part of these statements.

South Durango Sanitation District

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

For the years ended December 31,

	2018	2017
Operating Revenues		
Charges for services	\$ 619,390	\$ 607,826
Operating Expenses		
Collection and treatment	664,377	594,925
General and administrative	<u>187,128</u>	<u>173,875</u>
Total operating expenses	<u>851,505</u>	<u>768,800</u>
Operating income (loss)	(232,115)	(160,974)
Non-operating Revenues (Expenses)		
Tap fees	1,199,500	587,625
Investment earnings	17,468	5,159
Other income (expense)	-	120
Interest expense	<u>(35,054)</u>	<u>(72,229)</u>
Total non-operating revenues (expenses)	<u>1,181,914</u>	<u>520,675</u>
Net income (loss)	949,799	359,701
Net position at beginning of year	<u>5,630,262</u>	<u>5,270,561</u>
Net position at end of year	<u><u>\$ 6,580,061</u></u>	<u><u>\$ 5,630,262</u></u>

The accompanying notes are an integral part of these statements.

South Durango Sanitation District

STATEMENTS OF CASH FLOWS

For the years ended December 31,

	2018	2017
Cash Flows from Operating Activities		
Cash received from customers	\$ 617,578	\$ 614,688
Cash paid to suppliers	(486,186)	(431,922)
Cash paid to employees	(75,258)	(70,543)
Net Cash Provided (Used) by Operating Activities	56,134	112,223
Cash Flows from Non-capital Financing Activities		
Tap fees	1,199,500	587,625
Net Cash Provided (Used) by Non-capital Financing Activities	1,199,500	587,625
Cash Flows from Capital and Related Financing Activities		
Debt and capital lease principal payments	(945,353)	(613,214)
Interest on debt	(38,025)	(74,097)
Purchases of capital assets	(40,222)	(34,930)
Net Cash Provided (Used) by Capital and Related Financing Activities	(1,023,600)	(722,241)
Cash Flows from Investing Activities		
Sale (purchase) of investments	(59,725)	(215,767)
Interest income	17,468	5,159
Net Cash Provided (Used) by Investing Activities	(42,257)	(210,608)
Net Cash Increase (Decrease)	189,777	(233,001)
Cash at beginning of year	71,028	304,029
Cash at end of year	\$ 260,805	\$ 71,028
Reconciliation of Operating Income to Net		
Cash Provided by Operating Activities		
Net operating income (loss)	\$ (232,115)	\$ (160,974)
Items to reconcile operating income to cash provided (used) by operating activities		
Depreciation	308,580	307,170
Other income (expense)	-	120
(Increase) Decrease in accounts receivable	(3,279)	5,206
(Increase) Decrease in due from Loma Linda Sanitation District	258	(3,782)
(Increase) Decrease in due from / to developers	(10,677)	(2,624)
Increase (Decrease) in accounts payable, net of noncash capital and investing activities	(11,152)	(34,429)
Increase (Decrease) in accrued payroll	3,052	-
Increase (Decrease) in revenue received in advance of service	1,467	1,536
Total Adjustments	288,249	273,197
Net Cash Provided (Used) by Operating Activities	\$ 56,134	\$ 112,223

The accompanying notes are an integral part of these statements.

South Durango Sanitation District
NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE A – DEFINITION OF REPORTING ENTITY

The South Durango Sanitation District (the District) was formed November 9, 1983, for the purpose of providing sanitation services for the residents and businesses located within the District. The District has its own governing board which is elected by eligible voters of the District.

The District is not financially accountable for any other organization, nor is the District a component unit of any other primary governmental entity.

The District follows the Governmental Accounting Standards Board (GASB) accounting pronouncements which provide guidance for determining which governmental activities, organizations and functions should be included within the financial reporting entity. GASB pronouncements set forth the financial accountability of a governmental organization's elected governing body as the basic criterion for including a possible component governmental organization in a primary government's legal entity. Financial accountability includes, but is not limited to, appointment of a voting majority of the organization's governing body, ability to impose its will on the organization, a potential for the organization to provide specific financial benefits or burdens, and fiscal dependency.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of the District's significant accounting policies is presented to assist the reader in interpreting the financial statements and other data in this report. The policies are considered essential and should be read in conjunction with the accompanying financial statements.

The accounting policies of the District conform to generally accepted accounting principles as applicable to governmental units accounted for as proprietary enterprise funds. The enterprise fund is used since the District's powers are related to those operated in a manner similar to a private business enterprise where net income and capital maintenance are appropriate determinations of accountability.

The more significant accounting policies of the District are described as follows:

Proprietary Fund

Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (including depreciation) of providing goods and services to the general public on a continuing basis be financed or recovered primarily through user charges. The District's operations are accounted for as one enterprise fund.

South Durango Sanitation District
NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Basis of Accounting

The District's records are maintained on the accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized when the liability is incurred. Unbilled sewer system utility service receivables are recorded at year end. Penalties, interest, and miscellaneous revenues are recorded when received in cash because they are generally not measurable until actually received. Depreciation is computed and recorded as an operating expense. Expenditures for property, plant and equipment are shown as increases in assets. Tap fees received are recorded as non-operating revenues.

Budgets and Budgetary Accounting

The District's Board follows these procedures in establishing the budget for the year:

1. In accordance with State statutes, prior to October 15, the person designated by the Board of Directors submits to the Board of Directors a proposed operating budget for the calendar year commencing the following January 1. The operating budget includes proposed expenditures and the means to finance them for the upcoming year, along with estimates for the current year and actual data for the preceding year. The state statutes require more detailed line item budgets be submitted in summary form. In addition, more detailed line item budgets are included for administrative control. The level of control for budgetary purposes is at the fund level.
2. Public hearings are conducted to obtain public comment.
3. Prior to December 31, the budget is legally enacted through passage of a resolution.
4. The person designated by the Board is required to present a monthly report to the Board of Directors explaining any variance from the approved budget.
5. State statutes require the adoption of a summary budget for proprietary funds.
6. Appropriations lapse at the end of each calendar year.
7. The District Board may authorize supplemental appropriations during the year.

Deposits and Investments

Colorado law authorizes the District to invest in obligations of the United States, State of Colorado, Colorado counties and school districts, repurchase agreements, financial institutions, and local government investment pools. House bill 1056 expanded the list of investments that are legal for local governments.

South Durango Sanitation District
NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Cash and Cash Equivalents

For purposes of the Statement of Cash Flows, the District considers all highly liquid investments purchased with a maturity of twelve months or less to be cash equivalents.

Prepaid Items

Payments made for services that will benefit periods beyond the end of the current year are recorded as prepaid items.

Allowances for Uncollectibles

No allowance for uncollectibles has been provided because the District has a statutory lien against the property served for all unpaid charges. The Board of Directors of the District believes it will collect on all past due accounts because by statute the lien is perpetual until paid.

Inventories

Inventories are stated at cost.

Fixed Assets

All fixed assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Donated fixed assets are valued at their estimated fair value on the date donated.

Depreciation of all exhaustible fixed assets used by proprietary funds is charged as an expense against their operations. Accumulated depreciation is reported on the statement of net position. Depreciation has been provided over the estimated useful lives using the straight line method. The estimated useful lives range from 5 to 40 years.

Net Position

Net position is reported as restricted when there are limitations imposed on its use either through the enabling legislation adopted by the District or through external restrictions imposed by creditor, grantors, or laws or regulations of governments. The District's policy with regard to the order of spending is to spend the restricted funds first

South Durango Sanitation District

NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Operating Revenues and Expenses

The District distinguishes between operating revenues and expenses and non-operating items in the Statements of Revenues, Expenses and Changes in Net Position. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the District's purpose of providing sanitation services to its customers. Operating revenues consist of charges to customers for service provided. Operating expenses include the cost of service, administrative expenses, and depreciation of assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

NOTE C – CASH AND INVESTMENTS

Cash is stated at cost, which approximates fair value, and consists of cash in checking and certificates of deposit. Investments consist of money market accounts, Colotrust, and CSAFE. The differences between the carrying amount and the bank balances are due to outstanding checks and deposits not yet processed by the bank.

Balances in these accounts at December 31, 2018 and 2017, are as follows:

	2018			2017		
	Carrying Amount	Insured Bank Balance	Collateralized Bank Balance	Carrying Amount	Insured Bank Balance	Collateralized Bank Balance
Cash and cash equivalents	\$ 260,805	\$ 304,472	\$ -	\$ 71,028	\$ 97,556	\$ -

The Colorado Public Deposit Protection Act (PDPA) requires that all units of local government deposit cash in eligible public depositories, the eligibility of which is determined by state regulators. Amounts deposited in excess of the federal insurance level must be collateralized. The eligible collateral is determined by the PDPA. The PDPA allows the institution to create a single collateral pool for all public funds. The market value of the collateral must be at least 102% of the aggregate uninsured deposits.

Pledged collateral must be held in an escrow account with another financial institution approved by the state banking commission. The pledged collateral cannot be released unless approval is obtained from the banking commission.

South Durango Sanitation District
NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE C – CASH AND INVESTMENTS – CONTINUED

Investments

Governmental Accounting Standards Board Statement No. 40, Deposit and Investment Risk Disclosure (GASB 40) establishes disclosure requirements related to investment risks including credit risk, custodial risk, interest rate risk and foreign currency risk.

Colorado state statutes authorize the District to invest in U.S. Treasury bills, obligations of any other U.S. agencies, obligations of the World Bank, general obligation bonds of any state or any of their subdivisions, revenues bonds of any state or any of their subdivisions, bankers acceptance notes, commercial paper, repurchase agreements, money market funds and guaranteed investment contracts. All investments must be held by the District, in their name, or in custody of a third party on behalf of the local government.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation.

Custodial Credit Risk

The custodial credit risk for deposits is the risk that, in the event of a bank failure, the District will not be able to recover deposits or will not be able to recover collateral securities that are in possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investments or collateral securities that are in the possession of an outside party. The District's deposits are either covered by depository insurance or all collateralized under the Colorado Public Deposit Protection Act and are therefore not deemed to be exposed to custodial credit risk. The District's investments are not deemed to be exposed to custodial credit risk because they are held by the District or by the District's custody agent in the District's name.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The District places no limit on the amount the District may invest in any one issuer.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

South Durango Sanitation District

NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE C – CASH AND INVESTMENTS – CONTINUED

The District has invested \$378,502 (2018) and \$318,777 (2017) in the Colorado Local Governmental Liquid Asset Trust, (Colotrust), an investment vehicle established for local government entities in Colorado to pool surplus funds. Colotrust operates similarly to a money market fund and each share is equal in value to \$1.00. A designated custodial bank provides safekeeping and depository services to Colotrust in connection with the direct investment and withdrawal functions. Substantially all securities owned by Colotrust are held by the Federal Reserve Bank in the account maintained for the custodial bank. The custodian's internal records identify the investments owned by Colotrust.

Colotrust funds carry a Standard and Poor's AAAM rating. The custodian's internal records segregate investments owned by the Trust. Colotrust records their investments at amortized cost and the District records its investment in Colotrust using the amortized cost method. There are no unfunded commitments, the redemption frequency is daily, and there is no redemption notice period. There is no custodial, interest rate or foreign currency risk exposure.

The Districts investments consisted of:

	<u>2018</u>	<u>2017</u>
ColoTrust	<u>\$378,502</u>	<u>\$318,777</u>
Total	<u><u>\$378,502</u></u>	<u><u>\$318,777</u></u>

NOTE D – TAX SPENDING AND DEBT LIMITATIONS

Colorado voters passed an amendment to the State Constitution, Article X, Section 20, which has several limitations, including revenue raising, spending abilities, and other specific requirements of state and local governments. The amendment is complex and subject to judicial interpretation. The District qualifies as an "Enterprise" because it is a government owned business authorized to issue revenue bonds and it receives less than 10% of its annual revenue in grants from state and local grants. It is therefore exempt from some provisions of the 1992 amendment. The District believes it is in compliance with the requirements of the amendment. However, the District has made certain interpretations of the amendment's language in order to determine its compliance.

South Durango Sanitation District
NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE E – LONG TERM DEBT

	<u>2018</u>	<u>2017</u>
Series 2006 revenue bonds	\$ -	\$ 855,000
CWRPDA note payable	<u>596,581</u>	<u>633,168</u>
	596,581	1,488,168
Less current portion	<u>37,322</u>	<u>171,586</u>
Noncurrent portion	<u><u>\$ 559,259</u></u>	<u><u>\$1,316,582</u></u>

Changes in long-term debt for 2018 follow:

	<u>Beginning Balance</u>	<u>Additions (Deletions)</u>	<u>Principal Payments</u>	<u>Ending Balance</u>	<u>Within One Year</u>
Series 2006 revenue bonds	\$ 855,000	\$ -	\$855,000	\$ -	\$ -
CWRPDA note payable	<u>633,168</u>	<u>-</u>	<u>36,587</u>	<u>596,581</u>	<u>37,322</u>
Total	<u><u>\$1,488,168</u></u>	<u><u>\$ -</u></u>	<u><u>\$891,587</u></u>	<u><u>\$ 596,581</u></u>	<u><u>\$ 37,322</u></u>

Changes in long-term debt for 2017 follow:

	<u>Beginning Balance</u>	<u>Additions (Deletions)</u>	<u>Principal Payments</u>	<u>Ending Balance</u>	<u>Due Within</u>
Series 2006 revenue bonds	\$ 1,380,000	\$ -	\$525,000	\$ 855,000	\$135,000
CWRPDA note payable	<u>669,034</u>	<u>-</u>	<u>35,866</u>	<u>633,168</u>	<u>36,586</u>
Total	<u><u>\$2,049,034</u></u>	<u><u>\$ -</u></u>	<u><u>\$560,866</u></u>	<u><u>\$1,488,168</u></u>	<u><u>\$171,586</u></u>

South Durango Sanitation District
NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE E – LONG TERM DEBT – CONTINUED

Revenue Bonds Series 2006

On December 28, 2006, the District issued \$2,000,000 of Revenue Bonds.

The interest rate is recalculated each year on the first day of every calendar year which will be 300 basis points below the rate publicly announced by JP Morgan Chase Bank at its principal office in New York as its principal office in the City of New York. The interest rate will not be less than 4% per annum and shall not be in excess of a maximum net effective rate of 12% per annum. The bonds were redeemed in full during 2018.

CWRPDA Note Payable

On May 15, 2012, the District obtained an \$800,000 loan from the Colorado Water Resources and Power Development Authority to expand the capacity of the District's wastewater treatment facility.

The loan bears interest at 2% per annum and requires semi-annual principal and interest payments through November, 2032. The loan is secured by a lien on the District's wastewater treatment facility.

The loan agreement contains a rate covenant requiring that the District establish rates, fees, and charges to generate revenues sufficient to pay all operation and maintenance expenses, provide for 110% of the debt service due for the year for the CWRPDA note payable and any other obligations with wastewater treatment facility liens on parity with the CWRPDA note, provide for required additions to any debt service reserve account for the CWRPDA note and any other obligations with wastewater treatment facility liens on parity with the CWRPDA note, provide for the debt service on any obligations secured by a subordinate lien on the wastewater treatment facility, and provide amounts necessary to pay and discharge all other charges and liens payable from gross revenues for the year.

The loan requires the establishment of an operations and maintenance reserve fund in an amount equal to three months of operation and maintenance expenses, excluding depreciation.

South Durango Sanitation District
NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE E – LONG TERM DEBT – CONTINUED

The following is a summary of the debt service requirements to maturity on the District's CWRPDA note payable:

Year	Principal	Interest	Total
2019	\$ 37,322	\$ 11,746	\$ 49,068
2020	38,073	10,995	49,068
2021	38,837	10,231	49,068
2022	39,619	9,449	49,068
2023	40,415	8,653	49,068
2024-2028	214,589	30,751	245,340
2029-2032	187,726	8,546	196,272
	<u>\$ 596,581</u>	<u>\$ 90,371</u>	<u>\$ 686,952</u>

NOTE F – CAPITAL LEASE OBLIGATION

NBH Bank Lease Purchase

On June 24, 2016, the District entered into a \$392,250 lease purchase agreement to finance the purchase of equipment.

The lease purchase agreement bears interest at 2.68% per annum and requires quarterly principal and interest payments of \$15,411 through June, 2023. The lessor owns the equipment until the obligation is satisfied in full. Though the lease payments are subject to annual appropriation, accounting standards require that the principal portion of future scheduled payments be presented as a liability of the District.

Equipment capitalized related to this lease purchase obligation amounts to \$392,250, with accumulated depreciation of \$49,031 at December 31, 2018. Amortization of this asset is included with depreciation expense.

The following is a schedule of the changes in the capital lease obligation for 2018:

	Beginning Balance	Additions (Deletions)	Principal Payments	Ending Balance	Within One Year
NBH Bank lease purchase	\$314,249	\$ -	\$ 53,766	\$260,483	\$ 55,213

South Durango Sanitation District
NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE F – CAPITAL LEASE OBLIGATION – CONTINUED

The following is a schedule of the changes in the capital lease obligation for 2017:

	Beginning Balance	Additions (Deletions)	Principal Payments	Ending Balance	Within One Year
NBH Bank lease purchase	\$366,597	\$ -	\$ 52,348	\$314,249	\$ 53,757

The following reflects future scheduled payments of the capital lease obligation:

Year	Scheduled Payments
2019	\$ 61,644
2020	61,644
2021	61,644
2022	61,644
2023	30,822
	<u>\$ 277,398</u>
Less amount representing interest	16,915
Principal portion of capital lease obligation	<u><u>\$ 260,483</u></u>

NOTE G – CAPITAL ASSETS

A summary of changes in capital assets during 2018 is as follows:

	Beginning of Year	Additions	Adjustments / Deletions	End of Year
Non-depreciable assets:				
Land	\$ 243,120	\$ -	\$ -	\$ 243,120
Depreciable assets:				
Furniture and fixtures	5,035	-	-	5,035
Equipment	576,312	14,072	-	590,384
Well	15,124	-	-	15,124
Storage building	20,828	-	-	20,828
Plant and improvements	10,637,715	26,150	-	10,663,865
	<u>11,498,134</u>	<u>40,222</u>	<u>-</u>	<u>11,538,356</u>
Less accumulated depreciation	4,443,423	308,580	-	4,752,003
	<u><u>7,054,711</u></u>	<u><u>\$(268,358)</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 6,786,353</u></u>
Net Utility Plant in Service	<u><u>\$ 7,054,711</u></u>	<u><u>\$(268,358)</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 6,786,353</u></u>

South Durango Sanitation District
NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE G – CAPITAL ASSETS – CONTINUED

A summary of changes in capital assets during 2017 is as follows:

	Beginning of Year	Additions	Adjustments / Deletions	End of Year
Non-depreciable assets:				
Land	\$ 243,120	\$ -	\$ -	\$ 243,120
Depreciable assets:				
Furniture and fixtures	5,035	-	-	5,035
Equipment	575,712	-	600	576,312
Well	15,124	-	-	15,124
Storage building	-	20,828	-	20,828
Plant and improvements	10,624,213	14,102	(600)	10,637,715
	11,463,204	34,930	-	11,498,134
Less accumulated depreciation	4,136,253	307,170	-	4,443,423
Net Utility Plant in Service	<u>\$ 7,326,951</u>	<u>\$(272,240)</u>	<u>\$ -</u>	<u>\$ 7,054,711</u>

NOTE H – TAP PURCHASE AGREEMENT

The District entered into a tap purchase agreement with the Tierra Group, LLC and its anticipated successor, GRVP, LLC (Developer), both of whom are wholly owned subsidiaries of the Southern Ute Indian Tribe (the Tribe) on April 16, 2004. This agreement grants the Developer exclusive right to purchase 490 taps between 2004 and 2009. The agreement also required the Developer to purchase taps when requested by the District (Guaranty Taps) when tap sales did not provide sufficient funds for payment of debt service on the District's 2004 revenue bonds. The Developer purchased 182 Guaranty Taps from the District which were assigned to various lots as development occurred. The final Guaranty Tap owned by the Developer was assigned in 2015.

The agreement recognizes the credit enhancement provided by the Tribe, which enabled the District to obtain funds necessary to complete Phase 1 of the Wastewater Treatment Plant and the Grandview Interceptor. In recognition of that enhancement, the District agreed to guarantee the Developer exclusive right to 40% of the capacity in the interceptor.

South Durango Sanitation District

NOTES TO FINANCIAL STATEMENTS

December 31, 2018 and 2017

NOTE I – RISK OF LOSS

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters for which the District carries insurance. The District is insured for property, general liability, miscellaneous property and public official liability through membership in the Colorado Special District Property and Liability Insurance Pool (CSDPLP). The CSDPLP has a legal obligation for claims against its members to the extent that funds are available in its annually established loss fund and amounts are available from insurance providers under excess specific and aggregate insurance contracts. Losses incurred in excess of loss funds and amounts recoverable from excess insurance are direct liabilities of the participating members. The CSDPLP has indicated that the amount of any excess losses would be billed to members in proportion to their contributions in the years such excess occurs, although it is not legally required to do so. Ultimate liability to the District resulting from claims not covered by CSDPLP is not presently determinable. There were no material reductions in insurance coverage provided to the District and any amounts of settlements have not exceeded insurance coverage for the past three years.

CSDPLP has contracted with other third parties to operate, administer and manage the Pool. The Pool is responsible for its own budgets. CSDPLP's summary audited financial information as of December 31, 2017 (the most recent available), is as follows:

Assets	<u>\$56,602,888</u>
Liabilities	<u>\$30,815,521</u>
Surplus	<u>25,787,367</u>
	<u>\$56,602,888</u>
Revenues	\$20,713,694
Expenses	<u>18,721,378</u>
Net Income (Loss)	<u>\$ 1,992,316</u>

SUPPLEMENTAL INFORMATION

South Durango Sanitation District

SCHEDULE OF OPERATING EXPENSES

For the years ended December 31,

	2018	2017
Collection and treatment		
Depreciation	\$ 308,580	\$ 307,170
System maintenance	98,802	87,390
Employee payroll	78,310	70,543
Engineering costs	77,957	33,067
Utilities	72,089	70,143
Insurance	15,803	15,155
Chemical testing	12,836	11,457
Total collection and treatment	<u>\$ 664,377</u>	<u>\$ 594,925</u>
General and Administrative		
Accounting and legal	\$ 98,544	\$ 82,558
Operators	37,500	37,500
Payroll tax expense	22,363	23,688
Postage and office	17,542	16,793
Board of directors	6,615	5,598
Other	3,496	5,982
Dues and licenses	1,068	1,756
Total general and administrative expenses	<u>\$ 187,128</u>	<u>\$ 173,875</u>

South Durango Sanitation District

SCHEDULE OF EXPENSES - BUDGET AND ACTUAL

For the years ended December 31, 2018 and 2017

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Expenditures Reported on the GAAP Basis</u>	<u>Adjustments to Budgetary Basis</u>	<u>Expenditures on the Budgetary Basis</u>	<u>Variance with Final Budget Favorable (Unfavorable)</u>
2018						
Total expenditures	\$ 1,735,821	\$ 1,735,821	\$ 886,559	\$ 676,995	\$ 1,563,554	\$ 172,267
2017						
Total expenditures	\$ 771,021	\$ 1,182,003	\$ 841,029	\$ 340,974	1,182,003	-

Adjustments to budgetary basis are comprised of principal reductions on long-term debt, capital expenditures, and depreciation expense.

South Durango Sanitation District

SCHEDULE OF COLORADO WATER RESOURCES AND
POWER DEVELOPMENT AUTHORITY LOAN COMPLIANCE

For the year ended December 31, 2018

Rate Covenant

Gross Revenue:

Charges for services		\$ 619,390
Tap fees		1,199,500
Investment earnings		17,468
Other income		-
		<u>1,836,358</u>

Operation and maintenance expenses:

Total operating expenses	851,505	
Less depreciation expense	<u>(308,580)</u>	
		542,925

Current year debt service requirements for CWRPDA loan and
parity lien obligations:

2012 Colorado Water Resources and Power Development Authority Loan	49,068	
2006 Revenue Bonds	<u>169,200</u>	
	218,268	
Required coverage	<u>110%</u>	
		240,095

Current year required payments into debt service reserve account
for CWRPDA loan and parity lien obligations

-

Current year debt service requirements on subordinate lien
obligations

61,644

Current year debt service requirements on other obligations

-

844,664

Excess (deficiency) of gross revenues over covered expenses

\$ 991,694

Operations and Maintenance Reserve Covenant

Required reserve equal to three months operations and maintenance expenses	\$ 135,731
Restricted net position on the Statement of Net Position	135,731

Lien Representation

No new obligations with liens on the wastewater treatment facility were incurred during the year.